

GOVERNMENT OF THE DISTRICT OF COLUMBIA

Office of the Chief Financial Officer

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Office of Integrity and Oversight



MEMORANDUM

TO: Stephen Cordi, Deputy Chief Financial Officer
Office of Tax and Revenue

FROM: Robert G. Andary, Executive Director
Office of Integrity and Oversight

DATE: May 29, 2009

SUBJECT: Management Alert: Internal Control Weaknesses Identified in OTR's Processing of Receipts from the Collections Division's Post Office Box (IA:OTR:2907:C12(1))

The Office of Integrity and Oversight (OIO) is currently performing a review of the Office of Tax and Revenue (OTR) Compliance Administration Collections Division's (CD's) monthly collections data reported for the period October 1, 2005 through October 31, 2008. As part of this review, we conducted a "walk-through" of the collections receipts process within CD. In our walkthrough, we identified several weaknesses in the system of internal controls for the processing of receipts by CD. This management alert provides our findings and four recommendations to improve the system of internal control for these receipts.

OIO determined that CD did not have functioning internal controls to safeguard the receipts from the CD Post Office Box (POB). Further, controls were not in place to assure that the revenue officers (ROs) and tax examiners (TEs) processed POB receipts in compliance with the Office of the Chief Financial Officer's (OCFO's) policy of two days from the date of receipt of the funds.

Background

CD maintains a separate POB from that of the Returns Processing Administration (RPA) to collect tax receipts from individuals who have: (i) been referred to CD for delinquent payment of taxes,¹ and (ii) assigned to a specific RO or TE for collection action. Further, the POB takes in receipts from those taxpayers whose delinquent accounts have been assigned to a debt collector, under contract with CD. Additionally, the POB provides a location for taxpayers to mail correspondence to CD or a specific RO or TE.

The CD asserts that the POB allows them to better track the progress of their collection efforts, as a whole, and the collection efforts of a specific RO or TE. They further assert that the POB allows them to ensure that the funds received are identified as collections and credited to the proper taxpayer account, in cases where a taxpayer has multiple delinquent accounts. Furthermore, CD asserts by having the RO or

¹ The term tax, for this memorandum, does not include taxes on real property; which are processed through the Real Property Tax Administration.

TE complete the payment posting voucher (PPV) this reduces the time necessary to process individual payments within RPA, as the research work is already done and the RO or TE identified the proper account(s) for crediting.

The POB is the largest single receipt point for collections. With the exception of late returns CD asserts that the majority of the delinquent tax receipts come through the POB.

Absence of Controls for POB Receipts

OIO found the absence of a functional system of internal controls and procedures for the in-coming receipts and tracking of tax payments received through the POB. Taxpayer payments were not separately identified and tracked until the RO or TE delivered the payment to RPA for processing. We found that there was no system in place to ensure that all payments received on a specific date were distributed to the collection teams, processed as a contractor collection, or referred to a team or specific individual for resolution of a payment issue or question.

A sole clerical assistant (CA) is responsible for the pickup of the mail receipts, sorting and delivering those receipts to the respective collection teams, and processing the payments generated by the CD debt collection contractors. This function is rotated on a weekly basis among the CA's assigned to the Collections Division.

The current system does not follow the receipts from collection at the post office through final processing in the integrated tax system (ITS). Envelopes containing potential receipts are not logged or opened to: (i) determine whether they contain taxpayers' receipts, and (ii) the amount of the receipts. CD does not restrictively endorse checks² as they are received. Instead the checks are not endorsed until they reach RPA for processing. The current process may require the check to pass through five different individuals before it is endorsed and tracked in RPA. This significantly increases the chances for the payment to be lost, manipulated, or diverted by a number of different individuals. The current system does not provide accountability for the receipts, and the only individuals that CD can reasonably assure were involved in the processing, are the CAs who sort and distribute the receipts from the POB.

Internal controls over cash receipts are fundamental to management's accountability over cash and a basic requirement to "best practices" of management oversight. Without controls in this area, an organization's management has no assurance that it is receiving all of the payments directed to it. The U.S. Government Accountability Office (GAO), in its publication *Internal Control Standards in the Federal Government (Standards)*, discusses the objectives of a system of internal controls. They state in part:³

"A subset of these objectives is the safeguarding of assets. Internal control should be designed to provide reasonable assurance regarding the prevention of or prompt detection of unauthorized acquisition, use, or disposition of agency's assets."

GAO also addresses the issue of controls for vulnerable assets in stating that:⁴

² The term checks for the purposes of this memorandum include personal and business checks, money orders, cashier and treasurer's checks, certified checks and other negotiable instruments. It does not include payments made in currency and coin.

³ U.S. Government Accountability Office, formerly the U.S. General Accounting Office; *Internal Control Standards for the Federal Government*; Report Number: GAO/AIMD-00.21.3.1; November 1999, page 5.

⁴ Ibid; page 15.

"Access to resources and records should be limited to authorized individuals, and accountability for their custody and use should be assigned and maintained. Periodic comparison of resources with the recorded accountability should be made to help reduce the risk of errors, fraud, misuse, or unauthorized alteration."

Based on the system in place in May 2009, CD cannot provide a reasonable assurance that all POB receipts are properly safeguarded, that the ROs and TEs process the receipts provided to them in accordance with OCFO policy, and that all other receipts received through the POB are processed timely. We found a more than remote possibility that payments could be lost, or manipulated with only a very limited possibility of detection by another CD employee.

The following describes the weaknesses we noted during our "walk-through" of the POB receipts process:

I. Absence of Documentation to Support the Controls of Taxpayer Receipts

OIO found that CD does not effectively document its POB receipts until the RO or TE sends the individual receipt and payment to RPA for processing. As noted before, this may take several days and the payment may pass through as many as five individuals without documentation. Only the CA who is responsible for the sorting and delivering of mail can be definitively determined, through the CD assignment sheet. The current CD process relies on the veracity of the individuals who receive the payments and the subsequent timely processing of those payments. The current practices provide more than a remote opportunity for payments to be lost, delayed in processing, or intentionally diverted.

The CA is not required to enter the payment data into a paper or electronic log or to identify specific payments that are sent to ROs and TEs within the various teams. This entire process is generally done solely by the individual CA with limited oversight. Sole responsibility for assuring that all POB receipts received that day are processed by the close of their tour of duty.

Once the mail has been delivered to the CA who supports the specific collection teams, the CA distributes the mail to the respective individual RO or TE for processing and preparation of a PPV for the payment they received. The RO or TE may make copies of the payments received and the resulting PPV for their records; however, this is not required by CD. The RO or TE may return the check and PPV to the CA or deliver it directly to RPA for processing. The only records maintained to this point are those voluntary records held by the individual RO or TE for the delinquent accounts they have been assigned. Further, until the receipt is entered into ITS by RPA, there is no formal record of the payment.

A basic tenet of a functional system of internal control for taxpayer checks is that control and tracking of the checks be established as soon as feasible and that controls for the handling and processing of the receipts be documented throughout the process. These controls provide an accountability trail of the individual(s) responsible for processing the receipt and provide a reasonable assurance of the time it takes to process an individual receipt. Accountability for payments is a critical component of any internal control system for cash receipts. Further, restricting access to the payments and the processing for those payments minimizes the chances for inadvertent or intentional loss of the payment or errors identifying the payment and the correct account to which it should be charged.

2. *Inadequate Separation of Duties*

OIO notes that the duties for processing the payments received from the POB rests solely with the CA who picks up the mail. Currently, a CA from CD is assigned on a weekly basis to:

- pick-up the mail from the POB;
- sort the mail for processing by the collection teams;
- deliver the sorted mail to the CA who supports the specific collection team;
- open the mail whose destination cannot be determined from the envelope and sort the mail to the appropriate collection team;
- open the mail from collection accounts, prepare PPVs for the payments received from taxpayers, and deliver the payments to RPA for processing; and
- resolve, with a supervisor, any questions regarding to whom a payment or correspondence should be referred.

It appears that no other individual verifies that all the payments received during a specific day have been appropriately distributed or that the PPVs are prepared. When a large number of payments are received, it appears that the CA is responsible for notifying a supervisor and requesting assistance to process the payments. The current process places almost exclusive reliance on the CA and does not account for errors in the processing of the mail which may significantly delay the processing of a taxpayer's payment. Further, the process does not provide reasonable assurance that all the payments received have been processed.

Separation of duties is a critical component of any system of internal control. GAO in its *Standards* publication states⁵:

"Key duties and responsibilities need to be divided or segregated among different people to reduce the risk of error or fraud. This should include separating the responsibilities for authorizing transactions, processing and recording them, reviewing the transactions, and handling any related assets. No one individual should control all key aspects of a transaction or event."

By separating duties CD management can provide reasonable assurance that all payments received through the POB are initially recorded and distributed to the collection teams for further processing. The separation allows for the responsibility for sorting and processing payments over a number of individuals, effectively spreading the workload among several individuals and not placing it solely in the hands of a single individual.

3. *Restrictive Endorsement of Taxpayer's Payments*

CD's POB receipt processing does not require the restrictive endorsement of a taxpayer's payment upon receipt. OIO found that payments were not endorsed until the check was processed by RPA in some cases this could be several days later. As we previously stated, a payment received through the POB may pass through up to five individuals without being restrictively endorsed. This process increases the potential for the check to be negotiated by an individual, who is not authorized to do so, and increases the possibility that should a check be lost or misplaced it could be negotiated by an unauthorized individual.

⁵ Ibid; page 14.

One of the fundamental principles of a sound system of internal controls is to protect vulnerable assets from unauthorized use or manipulation, or being unaccounted for. Placing restrictive endorsements on individual checks limits the ability of an individual to improperly negotiate a payment.

Recommendations

We recommend that the Director of the Compliance Administration implement the following recommendations to establish a reliable system of internal controls over OTR's POB receipts:

1. Develop a system that tracks the taxpayer's payments from the initial receipt from the POB through turning over the checks and related PPV to the RPA for processing. This system should provide for a separation of duties so that no single individual can control the entire transaction stream.
2. Develop a database or spreadsheet application to log receipts from the POB. This application should contain fields to capture the (i) taxpayer's name, (ii) taxpayer identification number or account number, (iii) the specific account that the payment is to be credited to, (iv) amount of the payment; (v) date the payment was received; and (vi) the RO, TE, or team to whom the payment was given.
3. Require that the CA sorting the mail from the POB to enter the payments into the database spreadsheet as the mail is being sorted.
4. Require that all checks be restrictively endorsed at the point of initial receipt by the CA processing the POB receipts.

Please provide a response to this Management Alert within fifteen (15) business days of receipt of this memorandum report. If you have any questions, please contact Mohamad Yusuff, Internal Audit Director at 442-8240, or Tisha Edwards, Audit Manager, at 478-9143.

cc: Glen Groff, Director of Operations, OTR
Bedell Terry, Director of Compliance, OTR
Portia Perry, Chief of Collections, OTR
Mohamad Yusuff, Internal Audit Director, OIO
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Tisha Edwards, Audit Manager, OIO

GOVERNMENT OF THE DISTRICT OF COLUMBIA

Office of the Chief Financial Officer

Office of Tax and Revenue



Stephen M. Cordi
Deputy Chief Financial Officer

MEMORANDUM

TO: Robert G. Andary, Executive Director
Office of Integrity and Oversight (OIO)

FROM: Stephen M. Cordi
Deputy Chief Financial Officer

DATE: July 17, 2009

SUBJECT: Management Alert: Internal Control Weakness Identified in OTR's
Processing of Receipts from the Collection Division's Post Office Box
(IA:OTR:2907:C12(1))

This is in response to your memorandum dated May 29, 2009, Report Number IA:OTR:2907:C13(1) in which you state that you identified an Internal Control Weakness in the Collection Division Processing of Receipts from its Post Office box.

We reviewed your report and agree with the conclusions.

In order to provide better separation of duties and insure the integrity of the receipt and accounting of payments we have revised the entire process as it relates to the PO Box for the Collection Division. The mail in the PO Box will no longer be picked up by the Collection Division. This responsibility has now been assigned to the Returns Processing Division. The new procedures will consolidate the receipt and processing of all mail in one place. The new procedures should also result in shorter deposit time for subsequent payments received by OTR from delinquent taxpayers. These procedures will be fully implemented by July 24, 2009.

A copy of the new procedures is attached for your information. If you have any questions or require additional information regarding our response or progress towards implementation please call me or have a member of your staff contact Glen Groff, Director of Operations, at (202) 442-6499.

cc: Glen Groff, Director of Operations, OTR
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**RETURNS PROCESSING ADMIN ISTRATION
PAYMENT PROCESSING**

A/R and Compliance Payment Processing

Background: Generally, taxpayers are mailing in payments for Accounts Receivables (A/R) or bills using one of the following methods:

1. Mailing in the payment with the bill (A/R) to the address on the bill which directs the mail to PO Box 419
2. Send the payment with the bill (A/R) or note to the 941 N. Capitol St address
3. Send the payment to PO Box 37759 which is the address provided for cases being handled by Collection.
4. Taxpayers also send payments to PO Box 556 which is designated for use for Audit work.

PO BOX	RETURN/DOCUMENT IDENTIFICATION
419	Revenue Officer's work - RPA Pick Up
556	Audit Division - RPA Pick up
37759	Collection Pick Up
	941 North Capitol St Address (white mail)

Payments received through PO Box 419, PO Box 556 and the 941 North Capitol St address is picked up daily by RPA and subjected to normal extraction and sorting. All mail addressed to a specific person or regarding a specific case is copied and forwarded to Compliance. Checks and the attachments are forwarded to Code and Edit Unit for additional processing. This processing involves the following:

1. For all A/R documents with scan line data, Code and Edit compares the check information to the A/R document. If in agreement, the A/R document and check are batched and sent to the deposit activity, using the NCR scanner, for deposit of the check and processing of the A/R document. Following scanning and deposit, the transaction is sent to the Data Repair unit for keying of the bill number and any other data not recognized during the scanning process. Once the A/R has been processed thru Data Repair, the payment can be applied to the taxpayers account.
2. For all A/R documents without a scan line present, Code and Edit will look to see if the check has period/tax information or the taxpayers account is reviewed to ensure we know the true tax period or tax type. After the tax type and tax period information is determined, the A/R document and check is batched and forwarded to normal processing using the NCR scanner system. Following scanning and deposit, the transaction is sent to the Data Repair unit for keying of the bill number and any other data not recognized during the scanning process. Once the A/R has been processed thru Data Repair, the payment can be applied to the taxpayers account.

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- 3. If the incoming check indicates the payment is for multiple tax periods or that it can not be determined what the payment is to be applied against, a copy of the check and correspondence (if any) is copied and transmitted to Compliance for proper posting information. Once Compliance has identified the correct posting information, Code and Edit will apply the payment based on the information supplied. These payments are treated as a Key Punch documents defined below.**

Payments mailed to PO Box 37759 are picked up by Compliance which subsequently provides the checks along with Payment Posting Vouchers (PPV) to define the proper allocation or tax period/tax type information to be associated with the check. Payment posting vouchers are received in the RPA receiving room and then controlled to Code and Edit. PPV's are processed using a procedure called "Key Punch". Key Punch processing involves keying data from the PPV into a system that produces a hard copy document which is submitted from processing, with the check attached thru Document Prep unit, into the Scanning unit, via Banktec scanners, back to the deposit activity and then into data repair all prior to posting of the money to the taxpayers account.

**RETURNS PROCESSING ADMINISTRATION
PAYMENT PROCESSING**

Proposed Processing Procedures:

- 1. Change Receipt and Control MOTR to provide instructions requiring RPA to pick up from all Post Office boxes including PO Box 37759.**
- 2. Payments received in PO Box 37759 will be merged with payments picked up from PO Box 419, PO Box 556, and the 941 North Capitol St address and subjected to normal extraction and sorting. All mail addressed to a specific person or regarding a specific case will be copied and forwarded to Compliance.**
- 3. The extraction and sorting unit with RPA will assign PO Box 37759 mail as one of its first priorities each day.**
- 4. Change the Code and Edit MOTR to indicate that checks and the attachments are forwarded to Code and Edit Unit who will use the following procedures:**
 - a. For all A/R documents with scan line data, Code and Edit compares the check information to the A/R document. If in agreement, the A/R document and check are batched and sent to the deposit activity, using the NCR scanner, for deposit of the check and processing of the A/R document. Following scanning and deposit, the transaction is sent to the Data Repair unit for keying of the bill number and any other data not recognized during the scanning process. Once the A/R has been processed thru Data Repair, the payment can be applied to the taxpayers account.**
 - b. For all A/R documents without a scan line present, Code and Edit will look to see if the check has period/tax information or the taxpayers account is reviewed to ensure we know the true tax period or tax type. After the tax type and tax period information is determined, the A/R document and check is batched and forwarded to normal processing using the NCR scanner system. Following scanning and deposit, the transaction is sent to the Data Repair unit for keying of the bill number and any other data not recognized during the scanning process. Once the A/R has been processed thru Data Repair, the payment can be applied to the taxpayers account.**
 - c. If the incoming check indicates the payment is for multiple tax periods or that it can not be determined what the payment is to be applied against, a copy of the check and correspondence (if any) is copied and transmitted to Compliance for proper posting information. An aging log will be noted to record the taxpayer's name and the date the copies were sent to Compliance. This log will be reviewed daily and any request older than three business days will be elevated to the Director or Deputy Director of Compliance. Once Compliance has identified the correct posting information, Code and Edit will apply the payment based on the information supplied. If the payment has been identified to one specific tax period or tax type and**

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- if the profile exists within IDCS, the payment will be processed using a D40P, D20/30P etc. If there is not a profile for the tax year specified, the payment will be processed using Key Punch procedures.
- d. If the incoming check indicates or Code and Edit research determines that the check is to cover multiple tax periods within one tax type, the payment will be applied using a "P" document for the oldest tax period and allowing the system to offset any overage to more current tax periods.
 - e. For all cases where the payment can be associated with a single tax account and where profiles exist, "P" documents will be used in lieu of key punch documents.

To ensure timely processing of checks received from PO Box 37759, RPA will follow the 48 hour deposit cycle policy which specifies the length of time allowed for each unit to process checks (see attached diagram). The 48 hour deposit time frame represents payments that do not require Compliance research.